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NFP Sector Tax Concession Working Group Secretariat
The Treasury
Langton Crescent
PARKES ACT 2600

Not for Profit Sector - Tax Concession Working Group Discussion Paper

Dear Sir/Madam

The Royal Automobile Association of SA Inc (RAA) thanks you for the opportunity to make a submission in response to the discussion paper (Discussion Paper) in relation to tax concessions for the not for profit (NFP) sector released by the NFP Sector Tax Concession Working Group (Working Group).

The RAA is an Australian association incorporated under the *Associations Incorporation Act 1985* (SA) which services the motoring-related needs of South Australians and residents of Broken Hill. The RAA has over 580,000 members and employs approximately 800 staff in branches throughout South Australia. Services include the provision of 24-hour emergency roadside assistance, insurance products, car battery replacement, car and home security services, travel agency services, maps, guidebooks and relevant information via its motoring magazine, which is supplied free to members.

The RAA is not a tax exempt organisation and according to its constitution, is not carried on for the purpose of profit or gain to individual members. RAA has dealings with members and non-members and applies the principle of mutuality to its activities to the extent that those activities relate to members.

Our comments in relation to the discussion paper released by the Working Group are therefore only concerned with Chapter 5 of the Discussion Paper, **Mutuality, Clubs and Societies**.

The principle of mutuality is a long established taxation principle, where the surplus arising from contributions to a common fund created by a group of people for a common purpose is not income for tax purposes.

Our view, in summary, is that the principle of mutuality should be retained. Our reasoning is provided below.

Concern with uncertainty and complexity in operation

One of the concerns raised in the discussion paper is in relation to the uncertainty and complexity in operation of the principle of mutuality, in some cases, such as the tracking mutual and non-mutual receipts.

In our view, there are two elements that give rise to complexity and uncertainty of applying the principle of mutuality.

Firstly, identifying mutual receipts requires judgement as the receipt needs to be associated with the surplus of the common fund contributed by the members and there must also be a reasonable relationship between contributors to the fund and participants in the surplus. For member based organisations with a range of dealings with members and non-members, it can be difficult to differentiate between receipts relating to dealings with members that are part of the surplus common fund. In our view, complexity in applying this principle should not be a basis for legislative change to the mutuality principle. Rather, we recommend guidance and clarification is provided to mutual organisations in relation to the identification of mutual receipts, to assist them to comply with the application of the mutuality principle.

The second element of complexity, in our view, relates to the capability of mutual organisations to have the systems and processes in place to accurately calculate the net surplus/loss arising from mutual dealings. In our view, the ability of mutual organisations and NFP's more generally to accurately deal with their tax compliance obligations is an ongoing issue that needs to be considered and addressed.

Some mutual organisations, such as the RAA have the systems and processes in place to identify mutual receipts and deductions. However, the restricting or modifying the application of the principle of mutuality, as contemplated by this Discussion Paper, should increase concerns around compliance because smaller member based organisations may come within the taxation system and may not have the systems and processes to comply with the complexity of the mutuality principle.

Competitive neutrality concerns over ability to provide discounted services.

The discussion paper notes competitive neutrality concerns where members of clubs carry out trading activities of members in competition with non-exempt businesses.

Members of the RAA pay a membership fee which entitles them to discounts on member services. Even though discounts are afforded to members for the acquisition of goods and services, the membership fees offset, to a large extent, any competitive advantage. Therefore, for many mutual organisations such as the RAA, the competitive advantage is negligible because members pay for the right to access discounted services.

Social policy concerns

The discussion paper notes social policy concerns around gambling and the provision of alcohol to members.

In our view, these concerns are targeted at certain industries. On the contrary, motoring bodies such as the RAA provide benefits to the motoring community through advocacy and other community based services.

In our view, policy initiatives should directly address those concerns rather than through removing a fundamental tax principle that might have broader application to situations where the community benefits.

Investment of surplus

The discussion paper raises concerns around the investment of surplus funds by some larger mutual organisation into capital projects to benefit temporary or instant members.

RAA's business strategy is to increase its membership base and to retain members for the long term. Part of this strategy is to increase the range of services available to members in line with the objects of the RAA, through the reinvestment of member surpluses.

In our view, the reinvestment of mutual surpluses into initiatives aimed at broadening the range of services to members should not give rise to any concern around the operation of the mutuality principle.

Q53: Should the mutuality principle be legislated to provide that all income from dealings between entities and their member is assessable?

In our view, the common law principle of mutuality should be retained for the following reasons:

- ▶ **The concerns raised in the Discussion Paper are not universally applicable** - The concerns around the operation of the principle of mutuality do not apply to all member based organisations. Therefore, there is no need for broad reform that impacts all mutual organisations.
- ▶ **Member dealings are not income** - The fundamental principle that member based organisations not be taxable on member contributions should be retained and not be altered. Member contributions are not income under ordinary concepts nor should they be statutory income.
- ▶ **Increased complexity and compliance cost** - A narrower legislative principle of mutuality through limiting deductions would add to complexity of the current operation of the principle of mutuality. Any proposed legislative change that is likely to bring smaller member based organisation into the Australian tax system should be reviewed as any such change will increase compliance costs for these organisations, possibly without any real benefit.
- ▶ **Overseas examples not necessarily applicable in Australia** - Any decision to follow the examples of New Zealand, USA and Canada to restrict the application of the principle of mutuality would need to be fully considered in light of the above. The Principle of Mutuality would appear to be operating effectively presently, so we do not see the need to introduce an arbitrary threshold such as the 75% rule discussed in the Discussion Paper, which might distort efficient tax outcomes that currently arise.

Summary regarding concerns raised in the Discussion Paper

The concerns set out in the Discussion Paper around the operation of the mutuality principle are, in our view, not applicable to all mutual organisations. We ask the Working Group to take this into consideration in formulating its recommendations. In particular, if there are concerns applicable to certain clubs or industries, we recommend policy initiatives are formulated that target those concerns, rather than applying broader reforms which impact other organisations which provide benefits to the community.

Also, member based organisations, such as the RAA, are prohibited from making distributions to members. Therefore, franking credits arising from the payment of income tax are accumulated by the organisation, rather than distributed to members. This would appear to be an inefficient outcome especially as the tax liability may have arisen in respect of dealings with members.

If you have any questions regarding this submission, please do not hesitate to contact me on (08) 8202 8359.

Yours faithfully,



David McGown
Group Chief Financial Officer